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On May 27, 2020, while outlining its new proposals for the next Multiannual Financial Framework (MFF) that will determine the budget of the EU for the next 7 years, the European Commission proposed that on top of the "normal" budget, there should be a temporary Recovery Fund of up to 750 billion euro; the Fund should be financed through bonds that the Commission would be authorized to issue. This proposal had been foreshadowed a few days earlier by a joint initiative from Angela Merkel and Emmanuel Macron, also indicating the creation of a "Recovery Fund" of 500 billion euro. If adopted, the fund would represent a game changer in the decade-long history of European integration. Even with the Recovery Fund's temporary character, the EU has never seen a similar display of solidarity and joint financial action. Although allowing European institutions to issue common bonds is not in itself a novelty, the scale of the proposed program is.

The two proposals have similarities and differences; for the purpose of this paper, let's only focus on some of them. They are both conceived within the MFF. The Franco-German proposal says that the reimbursement of the debt could imply the creation of the EU's new "own resources". The Commission proposal is more explicit. The bonds that the Commission would be allowed to issue would be backed by the common budget and repaid in 30 years starting from 2028. To make it possible, the ceiling of the revenues available to finance the EU budget would be raised temporarily to 2% of the European Union's GDP. The Commission also proposes that these revenues should come from new "own resources". This has led some commentators to argue that the EU could be approaching its "Hamilton moment". What does this mean?

In 1790 the newly born United States of America was in a fragile state. Not only England, the former colonial master, but also other European powers were waiting for the new entity to collapse, eager to share the spoils. One looming danger were the debts incurred by the former 13 colonies to finance their participation in the War of Independence. The problem was not only the amount of the debt, but the fact that it was unequally shared among them: heavier on the poorer northern States and lighter on the richer southern ones. Alexander Hamilton, Secretary of the Treasury, proposed to President Georges Washington and managed to persuade Congress to transfer that debt from the States to the Union, guaranteed by the federal budget. The reluctant southern States were convinced that the situation was serious enough for them to provide solidarity. They obtained in exchange that the nation's capital would be built in a territory within the State of Virginia, at that time the most prosperous and important state; the area surrounding the capital was to become the District of Columbia. With that agreement Hamilton had saved the Union and, so his enemies said, also his friends in the banks of New York (his constituency) and London. The increase in customs duties necessary to back the new federal debt was also useful to protect the Union's nascent industry, which was mainly concentrated in the north. It was, in all respects, a brilliant political achievement.

Until recently, outside America this crucial episode in the history of the US was only known to a few historians and some European federalists. It is not easy to mobilize emotions around a debt problem; unless of course it becomes overwhelming. As it happens, this is exactly the main problem in the EU today: a potentially huge debt unequally distributed among member states that threatens the very cohesion of the EU and the existence of the euro. It is a divergence that is likely to increase and could be fatal in a Union struggling with an unprecedented recession. Hamilton is therefore becoming a household name in the European debate. Is Europe facing its “Hamilton moment”? Unfortunately, the short answer is: not really. For one thing, nobody in Europe is proposing to mutualize the existing debt; but there are other important differences.

In order to accomplish his plan, Hamilton did not need to change the Constitution that already entrusted Congress with all the powers necessary to raise taxes. Nothing of this sort exists in the EU. Articles 310 to 312 of the treaty establish that the budget must be in balance; the resources that are necessary to finance it require unanimous approval and must be ratified by the Parliaments of the member states. In the history of democracies, the power to levy taxes is one of the main attributes of sovereignty and requires a high degree of legitimacy for the institutions that are entrusted with it. The difference between today’s EU and the US even in Hamilton’s times, is that the US was already a federation, while the EU is not (or not yet). It is easy to see that to change the treaty in order to give the EU institutions the power of taxation, there would need to be an institutional reform that is much more radical than anything attempted so far; a step that would amount to a breach with the gradualist incremental approach that has been applied to date. Are the member states ready to cross that bridge? At least for the time being nobody seems ready to even ask that question. It is nevertheless interesting to note that in presenting the joint proposal, Merkel felt it necessary to mention the need for more “political union”.

Some would say that all this is correct, but both the Commission and the Franco-German proposal suggest that the budget should be financed with “own resources”. Isn’t that a step towards Hamilton’s achievement? Yes and no. There are two concepts that should not be confused: that of an “autonomous fiscal capacity” of the EU institutions and that of “own resources”. As we have seen, the first would only be possible through a major institutional reform. What about the second? The language in the treaty that mentions “own resources” is ambiguous. Historians will remember that the words were introduced in the early 1970s at the insistence of France, which wanted to be sure that the financing of the Common Agricultural Policy, at that time by far the most important chapter of the budget, would not be held to ransom by annual decisions made by national Parliaments. The most common interpretation is that the budget should be financed from taxes wholly or in part earmarked for that purpose. In the beginning it was decided that custom duties (including levies on agricultural imports) should almost entirely go to the common budget. It made sense because in a custom’s union it is impossible to determine at the point of entry the final destination of imported goods. In the meantime, the member states had decided to introduce VAT as the main indirect tax for the whole EU and it looked logical that a small part of it could become a second “own resource”. Reality has been a bit different. The tax base of VAT, not to speak of the rates, was never fully harmonized; the different national systems are still full of exceptions and derogations. As a result, far from being a real “own resource”, VAT is little more than an alternative statistical method to allocate national contributions to the budget. An additional problem has been that, while VAT revenues broadly follow the evolution of GDP, the parallel is not precise and some member states started to object, saying that they were treated unfairly. The first to do so was the UK in 1975. When in the course of the 1990s the development of cohesion policies made it necessary to increase the size of the budget, it appeared that the most sensible solution was to reduce the share of VAT even further and use national contributions based on GDP as the main source of revenue. Does that mean that we are in breach of the treaty? Not really. It can be argued that national contributions could be assimilated to "own resources" because their payment to the budget is obligatory. No national Parliament could do to the EU what Trump threatens to do to the budget of the WHO. Markets would probably prefer an EU debt backed by a truly federal budget, but given the present institutional set up, what matters most for them is that the reimbursement is guaranteed; it doesn't make a great difference whether it comes from contributions calculated on the basis of national GDP, or from a share of a more or less harmonized tax.

There is an additional difficulty on the road to "own resources". In Hamilton's times the share of taxation in the economy was very small and it remained so until around the First World War. In today's EU fiscal pressure in almost all member states is between 40 and 50% of GDP. Increasing the tax burden is highly unpopular in all countries. It is therefore very difficult to introduce new sources of revenue for the benefit of the EU without decreasing other existing taxes, or taking revenues away from member states. It can of course be argued that common policies could produce better results with less money, but the costs and the benefits would not be evenly distributed; in addition, no level of government likes to give away its taxing power. The alternative is the politically popular option of "making the foreigners pay"; as we shall see, it is not as easy as it seems. Finally, the heritage of the long and painful controversy with the UK is still there. Whatever the type of the revenues earmarked for the EU, all member states will negotiate having in mind the projected net balance between what they pay and what they receive.

The introduction of new "own resources" would have an undoubted political and symbolic value. However, you don't introduce new taxes purely for a political reason. They must also respond to a fiscal logic and their benefits for the single market and the European economy must be proved. It is a test which any new proposal must pass before it is seriously considered. Even more so now in the context of a terrible recession in which the EU is confronted with the prospects of huge debts, the main imperative of the recovery process will be to reestablish the conditions of a robust growth. Other criteria also apply. It would be better to consider taxes whose revenue is not likely to decrease over time. Furthermore, the ideal candidates are taxes that can go to the common budget in their entirety and, like customs duties, cannot easily be allocated to member states.

The Commission's proposal contains a rather long shopping list, including some ideas already put forward in the past, but not very rich in details. Without them it is very difficult to assess the credibility of the estimate that they could provide an amount or additional money between 25 and 35 billion euro per year. They can be divided into two broad categories. The first is related to the "European green deal", a cornerstone of the Commission's economic strategy. One idea is to tax specific products or sectors. Non-recyclable plastic materials, as well as air and maritime transport, have long been symbolic targets of the militant environmental community. To tax them would make the EU popular in those circles. The problem is that a tax on non-recyclable plastic would not last long, since there are already regulations that provide for its gradual disappearance. Air and maritime transport are a more serious issue. Although a small part of the total, their contribution to the increase of carbon emission is unquestionable. However, they are among the sectors that are most severely hit by the recession. To sustain the recovery, it will also be necessary to revitalize tourism and more generally, international trade, which is difficult to do without a healthy air and maritime industry. As a result of the epidemic and the lockdown, many companies are nearly bankrupt and are being saved, even nationalized, by the state; their recovery will be long. In these conditions, it is difficult to understand the rationale behind new taxes.

Another proposal makes more sense: to base new European revenues on the "emission trading system" (ETS), the complex system of emission ceiling and tradable permits allocated to sectors and companies with the aim to sustain the target of zero emissions. One impact of the development of the ETS system will be to increase costs for some industrial sectors: steel, cement, aluminum and plastics are obvious examples. If, as is feared, the EU's main trading partners and competitors don't follow the EU on this course, the burden on European industry could become severe. It would therefore make sense to compensate it with a "carbon border tax" levied on imports. Should this happen, it would also be logical to make it an "own resource". The Commission is working on concrete proposals and it is too early to assess them. We know, however, that they face important technical hurdles. It will also be necessary to give substance to the pledge that the proposed tax will be compatible with the WTO. Even in this case, however, the EU should expect a political reaction from the rest of the world, including the US.

The second set of ideas can be grouped under the chapter "industrial policy". One proposal is to use as an "own resource" the output of a "digital tax". It has been discussed for a long time and some member states (France and Italy among others) have already moved in that direction without implementing it. On the one hand, it has a lot of political support; public opinion doesn't understand why digital giants like Google, Amazon, Facebook or Apple (the GAFAs) pay minimal amounts of taxes in the countries where they operate. On the other hand, the issue is full of technical hurdles. The origin of the problem is not only due to the differences in national tax systems, but also to the difficulty to account for the growing importance of immaterial assets such as intellectual property. The main problem is political because many, although not all, of the companies concerned are American. In order to avoid a conflict with the US, it has been decided to try and reach an international agreement in the OECD. Unfortunately, the prospects don't appear to be good. If the negotiations fail, the EU will have to decide if it wants to act alone. If such a tax is ever introduced, it could become an "own resource"; for this to happen, it should however be completely harmonized throughout the EU. The Commission also mentions a rather nebulous tax on "large companies that profit from the single market", which is too vague to be discussed at this stage. One interpretation is that it could represent a broader version of the "digital tax" in order to avoid the criticism that it targets American companies.

The Commission also mentions the "common corporate tax base". This issue is complicated by the tendency to mix three different problems. The practice of some member states is to apply discriminatory criteria that favor certain companies, or even tax evasion, in order to attract investment from multinational companies. These can, and it is increasingly the case, be censured by the Commission because they are against the treaty. The second is the difference in the rates that are applied. They now tend to converge at around 20%, but there are countries that apply considerably smaller rates. Harmonizing them would be unrealistic and probably not practical; among other reasons, it would require unanimity. Finally, there is the harmonization of the tax base. It has been debated for a long time without meaningful results, in part because of the fear that it could lead to a harmonization of the rates. There is no doubt that an agreement would be beneficial and it would add transparency in the working of the single market. In addition, it would facilitate the solution of controversies on the taxation of multinational companies and would make it easier to come to a consensus on the "digital tax". Harmonizing corporate taxation is much harder than doing it for VAT; even if the EU succeeds, many exceptions and derogations will probably remain. It is therefore difficult to see how it could provide a basis for a new "own resource".

The result of this analysis is that, as things stand, the two main serious candidates to join the list of "own resources" of the common EU budget are the border carbon tax and the digital tax. As we have seen, they are both controversial and still undefined. Their common feature is that they risk creating a conflict with the EU's trade partners, including the US. If and when the EU comes to that point, it is logical to imagine that it would want to avoid a conflict on two fronts and therefore, a choice will have to be made.

Come what may, negotiations on the new MFF are likely to take up the largest part, if not the rest, of this year. The list of serious political difficulties is long. It includes the usual suspects present in all similar discussions, with the addition of the size of the recovery fund, the balance between grants and loans, the criteria for the allocation and the issue of conditionalities (fiscal, economic and political). All participants will have to define their priorities. Will "own resources" be part of them? There can be doubts about it. On the one hand, the issue has a symbolic value. On the other, to agree on the precise definition of a border carbon tax and/or a digital tax, or indeed on any other still undefined idea, will take time. On the basis of the Commission's proposal, they would not be necessary before 2028, when the recovery bonds will start to be reimbursed. This gives the discussion more time, but it could also push the issue out of the list of priorities.

In conclusion, the EU is not approaching its "Hamilton moment", but rather, like the single market and the euro, a new and welcomed bold step in the gradual functionalistic logic that has prevailed since the beginning. In the meantime, the European Hamilton can wait. He should be patient and be careful to avoid being killed in a stupid duel like his American predecessor.